

SECTION 1. PURPOSE.

A grant by a private foundation to an individual for travel, study, or other similar purpose by such individual is a 'taxable expenditure' by the private foundation for purposes of the tax imposed by section 4945 of the Internal Revenue Code of 1954 unless such grant satisfies the requirements of section 4945(g) of the Code. Section 4945(d)(3). Such a grant, awarded on an objective and nondiscriminatory basis pursuant to a procedure approved in advance, by the Secretary or the Secretary's delegate, may satisfy the requirements of section 4945(g)(1) if it is demonstrated to the satisfaction of the Secretary or the Secretary's delegate that the grant is a scholarship or fellowship grant that is subject to the provisions of section 117(a) and is to be used for study at an educational institution described in section 151(e)(4).

Ruling requests seeking advance approval of procedures are to be submitted to Assistant Commissioner (Employee Plans and Exempt Organizations), Attention: E:EO:T, Washington, D.C. 20224, and should include the statements described in section 53.4945-4(d) of the Foundation Excise Tax Regulations.

The purpose of this Revenue Procedure is to provide guidelines to be used in determining whether a grant made by a private foundation under an employer-related grant program to an employee or to a child of an employee of the particular employer to which the program relates is a scholarship or fellowship grant subject to the provisions of section 117(a) of the Code.

If the private foundation's educational grants are not scholarships or fellowship grants subject to the provisions of section 117(a) of the Code and do not otherwise qualify under the provisions of section 4945(g)(2) or (3), they would be 'taxable expenditures' within the meaning of section 4945(d), and might, depending upon the circumstances, lead to a loss of the private foundation's exempt status. As hereinafter explained, grants made by a foundation under an employer related grant program to employees, or to children of employees, of the particular employer to which the program relates could fail to be section 117 scholarships or fellowship grants because, for example, the purpose of the program is to provide extra compensation, an employment incentive, or an employee fringe benefit for the employees generally or a particular class of employees. Such a purpose would not be consistent with the foundation's exempt purpose or the allowance of deductions under section 170 for contributions to it.

The guidelines are directed only to the foregoing question of qualification under section 117 of the Code. For example, they are not directed to whether the private foundation's employer-related grant program meets the rules of section 53.4945-4(b) of the regulations requiring that the foundation's program be consistent with its exempt status and the allowance of deductions to individuals under section 170 for contributions to the foundation and that the group from which grantees are selected is a 'charitable class.' The guidelines assume that those requirements have been met except insofar as

that conclusion may be affected by the failure of the educational grants to be scholarships or fellowships subject to the provisions of section 117(a) and the reason for such failure.

Thus, for example, these guidelines assume that the group of employees, or children of employees, from which grantees are to be selected is sufficiently broad so that the awarding of grants to members of such a group could be considered consistent with the fulfillment of a purpose described in section 170(c)(2)(B) of the Code and the group could be considered to be a charitable class.

In addition, these guidelines are not directed to whether or not, if programs permit disqualified persons to receive grants, such grants constitute taxable expenditures under section 4945 of the Code or subject the disqualified persons to tax under section 4941.

SEC. 2. APPLICATION OF GUIDELINES.

These guidelines apply to educational grants made on or after January 1, 1970, by a private foundation under an employer-related grant program to individuals who are employees, or the children of employees, of the employer to which the program relates.

An employer-related program is a program that treats some or all of the employees, or children of some or all of the employees, of a particular employer as a group from which grantees of some or all of the foundation's educational grants will be selected, limits the potential grantees for some or all of the foundation's grants to individuals who are employees, or children of employees, of a particular employer, or otherwise gives such individuals a preference or priority over others in being selected as grantees of such grants.

These guidelines apply only to cases in which the group of employees, or children of employees, of the particular employer to which the program relates, from which grantees are to be selected, is sufficiently broad so that the awarding of grants to members of such a group could be considered consistent with the fulfillment of a purpose described in section 170(c)(2)(B) of the Code and the group could be considered to be a charitable class.

SEC. 3. BACKGROUND.

Section 117 of the Code provides that gross income does not include any amount received as a scholarship or as a fellowship grant at an educational institution (as defined in section 151(e)(4)). Section 1.117-3 of the Income Tax Regulations states that a scholarship generally means an amount paid or allowed to, or for the benefit of, a student to aid that student in pursuing studies. A fellowship grant is defined as an amount paid or allowed to, or for the benefit of, an individual to aid the individual in the pursuit of study or research.

Section 1.117-4(c) of the regulations explains that any amount paid or allowed to, or on behalf of, an individual to enable that individual to pursue studies or research is

nevertheless not a scholarship or a fellowship grant for purposes of section 117 of the Code if such amount represents compensation for past, present, or future employment services or if such studies or research are primarily for the benefit of the grantor. In the context of section 1.117-4(c), 'benefit' is not limited to monetary gain. See Jerry S. Turem, 54 T.C. 1494 (1970). It may include anything that furthers a noneducational purpose of a grantor. By contrast, a grant made for the relatively disinterested purpose of financially assisting an individual to pursue an education for that individual's own benefit may qualify as a section 117 scholarship or fellowship. The determination must, of course, be made in light of all the relevant facts and circumstances.

When educational grants are made available by an employer to its employees on a preferential basis, the employer-employee relationship is immediately suggestive that the grant is compensatory. See *Bingler v. Johnson*, 394 U.S. 741 (1969), 1969-2 C.B. 17. Such preferential grants by an employer to the children of employees suggests a purpose to compensate or otherwise provide an employment incentive to the employee-parents. These suggestions are not dispelled simply because the grantor is an independent third party (for example, a foundation). The employer-related preferential treatment does not, of itself, further in any way the requisite (under section 117 of the Code) disinterested purpose of simply making it financially possible for individuals to obtain an education for their own personal benefit, and suggests the presence of a contrary purpose to provide extra compensation, an employment incentive, or an employee fringe benefit. If a grant program by a private foundation is designed or administered to that end, the grants made under it to the employees or their children will not be scholarships or fellowship grants subject to the provisions of section 117(a).

The Internal Revenue Service will not, however, treat a private foundation's program as designed or administered for such a purpose if the availability of grants to employees of their children fall outside the pattern of employment. In order to be outside the pattern of employment, the availability of grants to employees or their children under the program must be controlled and limited by substantial nonemployment related factors to such an extent that the preferential treatment derived from employment does not continue to be of any significance beyond an initial qualifier. Such qualification must not lead to any significant probability that employment will make grants available for a qualified employee or his or her children interested in applying for one. The Service will treat the grants as scholarships or fellowship grants subject to the provisions of section 117(a) of the Code if (1) the availability of the grants falls outside the pattern of employment, and (2) the grants do not otherwise represent compensation for past, present, or future services rendered or to be rendered the foundation or employer by the employees or their children, and (3) the grants are not for studies or research undertaken primarily for the benefit of the foundation or the employer or for some other purposes not sanctioned by section 117.

SEC. 4. GUIDELINES.

If a private foundation's program satisfies the seven conditions set forth in sections 4.01 through 4.07, below, and meets the percentage test described in section 4.08

applicable to grants to employees' children, or to grants to employees, or to both, as the case may require, the Service will assume the grants awarded under the program to employees, or their children, or to both (if the percentage test is met for each category) will be scholarships or fellowship grants subject to the provisions of section 117(a) of the Code.

If a private foundation's program does not satisfy one or more of the seven conditions set forth in sections 4.01 through 4.07, the Service will not issue a ruling that the grants awarded are scholarships or fellowship grants under section 117 of the Code.

If a private foundation's program satisfies the seven conditions set forth in sections 4.01 through 4.07 below, but does not meet the percentage test of section 4.08 applicable to grants to employees' children or to grants to employees, as the case may be, the question whether the grants, awarded to individuals in the category (children or employees) in respect of which the percentage test was not met, are scholarships or fellowship grants subject to the provisions of section 117(a) of the Code will be determined on the basis of all the facts and circumstances. In making this determination, the Service will consider as a substitute for the percentage test of section 4.08 all the relevant facts and circumstances to determine whether the primary purpose of the program is to provide extra compensation or other employment incentive, or whether the primary purpose is to educate recipients in their individual capacities. These facts and circumstances will be considered in the context of the probability that a grant will be available to any eligible applicant.

Such relevant facts and circumstances could include the history of the program (such as the source of the program's funding), the courses of study for which the grants are available, any eligibility requirements imposed by the program (other than employment of the applicants or their parents and the age and grade level prerequisites for the studies for which the grants are available), the publicity given the grant program, the degree of independence of the selection committee, the particular standards used for selection, the specific means used to determine whether those standards have been met, the precise nature of the employee limitation or preference, the number of grants available, the number of employees or their children who would be eligible for them, the percentage of eligible employees or their children applying for grants who normally (e.g. on an average basis), receive grants under the program, and whether and how many grants are awarded to individuals who do not qualify as employees or children of employees.

.01 Inducement

The programs must not be used by the employer, the private foundation, or the organizer thereof, to recruit employees or to induce employees to continue their employment or otherwise follow a course of action sought by the employer.

.02 Selection committee

Selection of grant recipients must be made by a committee consisting wholly of individuals totally independent (except for participation on this committee) and separate from the private foundation, its organizer, and the employer concerned. An individual who is a former employee of either the foundation or the employer concerned will not be considered totally independent. Such committees preferably should consist of individuals knowledgeable in the education field so that they have the background and knowledge to properly evaluate the potential of the applicants.

The forwarding of the selections by the independent selection committee to the employer or private foundation for the sole purpose of verifying the eligibility requirements and selection criteria followed by the committee in considering the candidates and in making its selection will not disqualify the program. Any public announcement of the awards, however, must be made by the selection committee or by the foundation.

Grants must be awarded solely in the order recommended by the selection committee. The number of grants to be awarded may be reduced but may not be increased from the number recommended by the selection committee. Only the committee may vary the amounts of the grants awarded.

.03 Eligibility requirements

The program must impose identifiable minimum requirements for grant eligibility. Such requirements must be related to the purpose of the program and in the case of scholarships must limit the independent selection committee's consideration to those employees, or children of employees, who meet the minimum standards for admission to an educational institution (as defined in section 151(e)(4) of the Code) for which the grants are available. No persons will be considered eligible if they would not reasonably be expected to attend such an institution, however, even if they meet such minimum standards.

If an employee must have been employed for some minimum period by the employer to which the program relates to be eligible to receive a grant, or to make that employee's children eligible to receive a grant, the minimum period of employment may not exceed three years. Moreover, eligibility must not be related to any other employment-related factors, such as the employee's position, services, or duties.

.04 Objective basis of selection

Selection of grant recipients must be based solely upon substantial objective standards that are completely unrelated to the employment of the recipients or their parents and to the employer's line of business. Such standards as, but not limited to, prior academic performance, performance on tests designed to measure ability and aptitude for higher education, recommendations from instructors or other individuals not related to the potential awardees, financial need, and conclusions drawn from personal interviews as to motivation and character, may be utilized.

.05 Employment

A grant may not be terminated because the recipient or the recipient's parent terminates employment with the employer subsequent to the awarding of the grant regardless of the reason for such termination of employment.

If a grant is awarded for one academic year and the recipient must reapply for a grant to continue studies for a subsequent year, the recipient may not be considered ineligible for a further grant simply because that individual or the individual's parent is no longer employed by the employer. If a grant is awarded for a period of more than one academic year, subject to renewal, the standards for renewal must be based solely upon nonemployment related factors such as need and maintenance of scholastic standards. Renewal may not be denied because the recipient or parent has previously terminated employment with the employer. In such case, the recipient or parent met the employment requirement at the time the grant was first awarded, and no further employment requirement can be effected at the time of each renewal.

At the time the grant is awarded or renewed, there must be no requirement, condition or suggestion, express or implied, that the recipient or parent is expected to render future employment services for the foundation or the employer, or be available for such future employment, even though such future employment is at the discretion of the foundation or the employer.

.06 Course of study.

The courses of study for which grants are available must not be limited to those that would be of particular benefit to the employer or to the foundation. If the courses of study for which grants are available include one or more that would be of such particular benefit, a grant may not be conditioned on the recipient choosing such a course of study; the recipient must have a free choice to use the grant in the pursuit of a course of study for which the grant is otherwise available that is not of particular benefit to the employer or to the foundation.

.07 Other objectives

The terms of the grant and the courses of study for which grants are available must meet all other requirements of section 117 of the Code and the regulations thereunder, and must be consistent with a disinterested purpose of enabling the recipients to obtain an education in their individual capacities solely for their personal benefit and must not include any commitments, understandings or obligations, conditional or unconditional, suggesting that the studies are undertaken by the recipients for the benefit of the employer or the foundation or have as their objective the accomplishment of any purpose of the employer or the foundation (even though consistent with its exempt status) other than enabling the recipients to obtain an education in their individual capacities and solely for their personal benefit.

.08 Percentage test

In the case of a program that awards grants to children of employees of a particular employer, the program meets the percentage test if the number of grants awarded under that program in any year to such children does not exceed 25 percent of the number of employees' children who, (i) were eligible, (ii) were applicants for such grants, and (iii) were considered by the selection committee in selecting the recipients of grants in that year, or 10 percent of the number of employees' children who can be shown to be eligible for grants (whether or not they submitted an application) in that year.

In the case of a program that awards grants to employees of a particular employer, the program meets the percentage test if the number of grants awarded under that program in any year to such employees does not exceed 10 percent of the number of employees who, (i) were eligible, (ii) were applicants for such grants, and (iii) were considered by the selection committee in selecting the recipients of grants in that year.

For the purpose of meeting these percentage tests, an employee or child of an employee will be considered eligible only if the individual meets all of the eligibility requirements imposed by the program and such requirements satisfy the conditions of section 4.03 of this Revenue Procedure. Renewals of grants awarded in prior years will not be considered in determining the number of grants awarded in a current year. Grants awarded to children of employees and those awarded to employees will be considered as having been awarded under separate programs for purposes of all of the requirements of this Revenue Procedure whether or not they are awarded under separately administered programs.